

DEPARTMENT OF FINANCE

915 L STREET
SACRAMENTO, CA 95814-3706



JUL 24 2000

July 20, 2000

Mr. Ralph Chandler, Executive Officer
California Integrated Waste Management Board
8800 Cal Center Drive
Sacramento, CA 95826

Dear Mr. Chandler:

MANAGEMENT LETTER—USED OIL RECYCLING FUND OPERATIONS

In conjunction with our audit of the Used Oil Recycling Fund's financial statements, we have audited a representative sample of Used Oil Recycling grants. The overall audit has been conducted under an interagency agreement between the Department of Finance, Office of State Audits and Evaluations (OSAE), and the California Integrated Waste Management Board (Board), agreement number IWM-C8016, since November 1998. During the course of the grant audits, we have routinely observed the practices followed by the Board's grant managers in monitoring and overseeing the grants' operations. Although the grant program is largely successful in achieving its goals, several observed practices run counter to the Board's published Procedures and Requirements.

The scope of our audits included a review of grant receipts and expenditures, internal control, and compliance with contract provisions. We selected 12 percent (\$7,778,361/\$65,362,314) of the total grant funds awarded during the fiscal years ending 1995, 1996, and 1997 for testing. The sample comprised 37 grants awarded to 25 grantees. We were unable to audit three grants due to the grantees' ceasing operations and/or a lack of supporting documentation, thus reducing our final audit count to 34 grants awarded to 22 grantees.

We believe the following conditions relative to the Board's grant management deserve your attention and comment.

- A. The Board did not always enforce compliance with the grant contracts' Administrative Procedures and Requirements, or Terms and Conditions, as described below. This lack of enforcement prevents the Board from effectively monitoring funds, and increases the risk of funds being used for unauthorized purposes.

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Incomplete Grant Contract Terms

The Board accepted incomplete grant application packages for four Grantees (18 percent), prior to awarding and issuing grant funds. For example, one Grantee was not required to submit all the participating city resolutions. Other Grantees were not required to include budget proposals or identify the grant project goals and tasks.

Non-compliance with the grant terms limits the Board's ability in determining the eligibility of proposed projects, obtaining assurance that grantees have authority from their governing bodies, and identifying the responsible parties. See Recommendation 1.

Incomplete Progress Reports

The Board did not always enforce compliance with grant reporting requirements. Grantees are required to submit quarterly progress reports until a project's completion. However, for nine Grantees (41 percent), we observed deficiencies in compliance with the reporting requirements. We found instances where reports were submitted two to nine months after the due dates. Additionally, we found instances where reports were not submitted and/or did not include all the required reporting elements. Not requiring Grantees to report on their progress impairs the Board's ability to effectively oversee grant expenditures or assess the achievement of grant goals. See Recommendation 1.

Unauthorized Budget Revisions

The Board approved reimbursements for twelve Grantees (55 percent), whose final payment requests included variances between the budgeted and actual cost categories. The grant Terms and Conditions state that if a Grantee needs to revise a budget, the Grantee shall notify the Board within ten working days. None of the reports reviewed included documentation indicating the Board approved the budget revisions. Unapproved deviations between budgeted and actual expenditures increase the risk that funds may not be expended as intended and prevent the Board from properly monitoring the projects' progression. See Recommendation 1.

Unauthorized Advertisements

The Board approved reimbursements for seven Grantees (32 percent) who did not obtain prior approval for public education, advertising, or promotional materials. The Administrative Procedures and Requirements state that Grantees must submit copies of public education, advertising, or promotional materials for review and approval by the Board prior to publication or distribution. Without pre-approval, the Board cannot determine if the published content of advertisements is in conflict with state or federal

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regulations, or acknowledges Board sponsorship; or if the expenditures are eligible for full or partial funding. See Recommendation 1.

Retention Fees Not Withheld

The Board did not withhold grant funds from five Grantees (23 percent), as required in the Administrative Procedures and Requirements. The Administrative Procedures and Requirements state that the Board "shall withhold and retain 10 percent (25 percent for 1996/97 grants) of the grant award until all conditions stipulated in the agreement have been satisfied." The Board's policy is to withhold the final 10 percent of the grant funds until approval of the final report and payment request. By not withholding funds, the Board's grant monitoring effectiveness is diminished. See Recommendation 2.

Reimbursement of Ineligible Expenditures

The Board inappropriately authorized reimbursements of ineligible expenditures, as outlined in the Administrative Procedures and Requirements, and Terms and Conditions. The ineligible expenditures included payments for services and products outside the grant period, for non-grant related items, for copies of contracts and purchase orders rather than invoices, and for invoices double billed by the Grantees. Seven Grantees (32 percent) were reimbursed a total \$181,989 for ineligible expenditures. Although the ineligible expenditures are immaterial in relation to the total grant funds tested ($\$181,989/\$7,778,361 = 2$ percent), the inadequate review of payment requests increases the risk of funds being used for unauthorized purposes and the potential for embarrassment to the Board and its grantees. See Recommendations 1 and 3.

Recommendations:

1. Ensure enforcement of all grant contract Administrative Procedures and Requirements, and Terms and Conditions. Any deviations should be documented, approved by the grant manager, and included in the Grantees' files.
2. Modify the Board's fund retention policy to withhold funds from each payment request, in an aggregate amount not to exceed 10 percent of the total grant award.
3. Strengthen controls over the payment request review process. Ensure that reimbursed expenditures are incurred within the grant period, supported by invoices, and claimed only once for reimbursement.

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- B. The Board inadequately monitored the distribution of advanced grant funds. For the years included in our audits, the Administrative Procedures and Requirements allow for grant funds' advances based on the Grantee's justification of need and the requirement that specific expenditures be incurred prior to or shortly after payment. Two Grantees (nine percent) requested and received advance funds for immediate needs but did not expend the funds upon receipt. These Grantees held the funds for seven to twelve months before expending them. As a result, the Board forfeited approximately \$3,000 in interest earnings. This forfeiture violates the State's policy of maximizing interest earnings (State Administrative Manual, Section 8099).

Additionally, beginning with the Used Oil Recycling Block Grants fifth cycle, commencing June 30, 1999, the Board began advancing 100 percent of block grant funds awarded. During this cycle, the Board advanced approximately \$24,535,350 in block grant funds. The State Contracting Manual, Section 7.2 states that the State may advance funds only as specifically authorized by statute. We could not, nor could Board staff, substantiate the Board's legal authority for advancing 100 percent of these funds. Advancing funds to Grantees without proper monitoring or authority results in lost interest to the State, diminishes the effectiveness of the Board's grant management oversight, and increases the risk of funds being used for unauthorized purposes.

Recommendation:

1. Revise grant agreements to allow fund advances only when specifically authorized and necessary for the achievement of grant objectives.

When advances are deemed necessary, ensure guidelines for the accounting of advances are included in grant agreements. Those guidelines should include requirements for timely advance expenditures, deposit of advances into interest bearing accounts, and expenditure of any interest earned on grant related activities.

2. Include a provision for retaining at least 10 percent of the total grant funds awarded until all conditions stipulated in the grant agreement have been satisfied.

Implementing the recommendations discussed above will help ensure that the Board's interests are addressed and that the Board's grant programs operate effectively and efficiently.

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Please provide your written response to this management letter within 10 working days of receipt. If you have any questions regarding this management letter or the grant audits, please contact Richard B. Smith, Manager, or Richard Hebert, Supervisor, at (916) 322-2985.

Sincerely,



Samuel E. Hull, Chief
Office of State Audits and Evaluations
(916) 322-2985

cc: Ms. Terry Jordan, Acting Deputy Director, Administration and Finance Division,
California Integrated Waste Management Board
Mr. Mark Leary, Deputy Director, Special Waste Division, California Integrated Waste
Management Board